

Office of Chief Counsel
Internal Revenue Service

memorandum

CC:NER:MAN:TL-N-5834-99
LDavidow/OMendiburt

date:

to: Chief, Examination Division, Manhattan District
Attn: Robert Gruska, Senior Reviewer, QMS Section A

from: District Counsel, New York CC:NER:MAN

subject:

I.R.C. § 6402 Interest Offsetting Issue

UIL Numbers: 6402.02-00

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We have been asked for assistance to determine whether the Service can offset reductions in interest in the taxable year ended December 31, [REDACTED] against interest assessed on a deficiency for the taxable year ended December 31, [REDACTED]. The advice rendered in this memorandum is conditioned on the accuracy of the facts provided to us.

Facts:

[REDACTED] (the "taxpayer") filed a claim for a refund of a portion of the interest assessed on its deficiencies for taxable years [REDACTED], [REDACTED], and [REDACTED] pursuant to *May Department Stores Co. v. United States*, 36 Fed. Cl. 680 (1996) and *Sequa Corporation v. United States*, 97-1 USTC ¶ 50,317 (S.D.N.Y. 1996). On July 29, 1999, District Counsel issued final advice to the Examination Division advising that the taxpayer is

entitled to a refund of interest based on its credit elect claim. As a result, the taxpayer has been determined to have overpaid \$ [REDACTED] of its liabilities for taxable year [REDACTED] as of [REDACTED]. However, the Service has not processed this overpayment or credited the taxpayer's [REDACTED] tax balance as of the drafting of this memorandum.

The taxpayer also requested that the Service offset its [REDACTED] overpayment against its [REDACTED] deficiency as of [REDACTED], instead of refunding the [REDACTED] overpayment. The taxpayer paid its liability for the [REDACTED] taxable year on December 31, [REDACTED]. Therefore, the potential period of offsetting interest begins on [REDACTED] and ends on December 31, [REDACTED].

Issue:

Whether the taxpayer is entitled to offset its [REDACTED] overpayment against liabilities that accrued on its [REDACTED] tax deficiency from [REDACTED] through December 31, [REDACTED].

Analysis:

Under I.R.C. § 6402, the Service "may credit the amount of such overpayment, including any interest allowed thereon, against any liability in respect of an internal revenue tax on the part of the person who made the overpayment." Treas. Reg. § 301.6402-1, which further elaborates this Code section, states that "[t]he Commissioner ... may credit any overpayment of tax, including interest thereon, against any outstanding liability for any tax (or for any interest ...) owed by the person making the overpayment...." (Emphasis added.)

In *Northern States Power Co. v. Commissioner*, 73 F.3d 764 (8th Cir. Minn. 1996), Northern States Power Co. ("NSP") attempted to offset its 1981 and 1982 overpayments against its 1980, 1983 and 1984 underpayments to avoid the gap in interest rates. The Court followed Treas. Reg. § 301.6402-1 by opining that the NSP's interest on its tax liabilities must be outstanding when the credit is made in order to be offset by overpayment interest. Despite arguments to the contrary, the Court decided to adopt the plain meaning of the statute. The Court reasoned that "only an outstanding liability can be 'satisfied' by a credit." Accordingly, since NSP paid its deficiencies in 1990 and the overpayment credit was made in 1994 there was no outstanding liability at the time of the credit and the taxpayer was not entitled to an offset.

Similarly, when the Service processes the overpayment for [REDACTED], the taxpayer's [REDACTED] tax liability will not be outstanding. The taxpayer satisfied its [REDACTED] liability on December 31, [REDACTED].

Therefore, the taxpayer's [REDACTED] overpayment may not offset its [REDACTED] tax and interest liability since the liability is not outstanding at the time of the credit.

Conclusion:

Based on the foregoing, we recommend that you disallow the offsetting of the taxpayer's [REDACTED] overpayment against its [REDACTED] liability, which was satisfied on [REDACTED].

If you have any questions regarding this matter, please contact Lawrence Davidow or Oleida Mendiburt of our office at (212) 264-5473, extension 241 or extension 233, respectively.

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